



INFRASTRUCTURE, GOVERNMENT &
HEALTHCARE

Ayrshire and Arran NHS Board

Annual audit report to Ayrshire
and Arran NHS Board and the
Auditor General for Scotland
2007-08

25 June 2008

AUDIT

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Notice: About this report

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's *Code of Audit Practice* ('the Code'). This report is for the benefit of only the Ayrshire and Arran NHS Board and is made available to Audit Scotland (together the beneficiaries), and has been released to the beneficiaries on the basis that wider disclosure is permitted for information purposes but that we have not taken account of the wider requirements or circumstances of anyone other than the beneficiaries.

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Executive summary

This report summarises our work for 2007-08 and findings in relation to our audit of the financial statements, corporate governance and performance management arrangements.

Financial statements

Following approval on 25 June 2008 we issued an audit report expressing an unqualified opinion on the financial statements for the year ended 31 March 2008 and on the regularity of transactions reflected in those financial statements.

Management considered and selected a combination of local and national assumptions in their calculation of the *Agenda for Change* accrual, which includes amounts due to 913 (whole time equivalents) staff not yet assimilated and the potential cost of successful reviews. The review process is at an early stage locally and nationally, so there is considerable uncertainty around the average success rate and therefore the impact on the financial position.

A contingent liability has been reported in respect of equal pay claims as cases are at too early a stage to allow an assessment of financial risk.

Corporate governance

We considered corporate governance arrangements as they relate to systems of internal control, the prevention and detection of fraud and irregularity, standards of conduct and arrangements for the prevention and detection of corruption, and its financial position.

The statement on internal control does not disclose any significant weaknesses in the systems of internal control; the content of the SIC is consistent with our understanding and is in accordance with Scottish Government guidance.

Internal audit have concluded that there is "*moderate assurance on the adequacy and effectiveness of the systems of internal control*".

There is a formal process to record, distribute and monitor action in response to key guidance and circulars, but changes in the year resulted in an incomplete register of guidance received.

The Board participated in NFI for the first time in 2007. We previously concluded that the Board had inadequate arrangements are in place for managing its obligations. Management has now established a formal process and has completed all high priority data matches, with the exception of one match currently under investigation.

The Board met all three financial targets for 2007-08.

The financial plan forecasts a break-even position in 2008-09 and an in-year excess of expenditure over resources of £3 million in 2009-10 to reduce the cumulative surplus to £7 million at 31 March 2010. The financial plan assumes 2% efficiency savings; achievement of which will be a significant challenge.

The capital plan for 2008-09 assumes that the Board will incur £37.2 million of capital expenditure. This includes £10.9 million of capital brokerage. The history of incurring significant capital expenditure in the last two months of the financial year (61.3% in 2007-08) creates a risk that management will not achieve the planned outturn.

Performance management

We considered Audit Scotland's priorities and risks framework areas in the planning phase of the audit. In April 2008 we completed a Best Value use of resources and financial management review for Audit Scotland that will be reported in 2008-09. We assessed the achievement of the efficient government savings and also considered the Board's role in the national shared support services consortium.

Development of acute services and mental health facilities will depend on achievement of financial plans and challenging efficiency targets. A culture change will be required to ensure that cash released through efficiency savings is directed and prioritised appropriately.

913 whole time equivalent staff (8%) were not assimilated by the year end. Assimilated staff have lodged 2,000 review requests, but management has not yet completed any reviews. There are significant workforce and financial challenges due to high absence levels. Management has developed a number of local initiatives to monitor the impact of sickness absence and 'promote attendance', but sickness absence rates remained high at 5.6%.

A 'strategic alliance' between the Board and three councils aims to improve partnership working at a strategic level. Management has prepared a draft engagement plan to outline key deliverables and milestones, to be developed further in the summer of 2008.

Management had identified significant risks to achievement of delayed discharge and three other key targets (staff absence, emergency re-admissions and cancer waiting times) in 2007-08. The corporate management team recognised that achievement of these targets required organisational commitment at all levels across all disciplines. While the delayed discharge target was achieved, the other 'at risk' targets were not.

Our review of the Board's information management arrangements confirmed that, subject to finalisation and implementation of information security management arrangements, processes are in place to mitigate key risks in this area.

Management established a 'benchmarking, efficiency and sustainability' team, responsible for providing leadership, direction and support for efficient government initiatives and projects, while balancing this with sustainability.

There is clear awareness and acceptance of competing financial and strategic pressures, but the way in which this change will be managed and implemented, strategically and financially, is not always clear and consistent across the organisation. Clear commitment and direction from top management will be crucial to the achievement of strategic and financial objectives in coming years.

Delays in identifying and implementing efficiency schemes will have a significant impact on the ability to meet 2% savings targets in 2008-09 and achievement will depend on implementation of a robust mechanism to identify, record and report savings achieved.

Introduction

Audit framework

This year was the second of our five-year appointment by the Auditor General for Scotland as external auditors of Ayrshire and Arran NHS Board ("the Board"). This report to the Board and Auditor General provides our opinion and conclusions and highlights significant issues arising from our work.

In accordance with Audit Scotland's Code of Audit Practice ("the *Code*") the scope of the audit was to:

- provide an opinion on the Board's financial statements and the regularity of your transactions;
- review and report on:
 - your corporate governance arrangements as they relate to: your review of systems of internal control; the prevention and detection of fraud and irregularity; standards of conduct, and prevention and detection of corruption; and your financial position
 - arrangements to achieve Best Value
 - other aspects of your arrangements to manage performance, as they relate to economy, efficiency and effectiveness in the use of resources.

We outlined the framework under which we operate, under appointment by Audit Scotland, in the audit plan discussed with the Board's audit committee.

Service overview

Following a consultation process and evaluation of models of emergency and unscheduled care stemming from a formal review of services, the board, and subsequently the (then) Scottish Minister for Health, approved a number of changes in service provision in October and December 2006. These changes focused on increased provision of services in the community and creation of five community casualty facilities. On 6 June 2007 the Cabinet Secretary for Health and Wellbeing announced the decision to reverse the previous Scottish administration's decision regarding the downgrading of accident and emergency services at Ayr Hospital. The Cabinet Secretary requested that the original plans be revisited and revised proposals produced that would enable accident and emergency services to continue at that hospital. As part of the review process, the Cabinet Secretary established an Independent Scrutiny Panel to review the revised proposals.

The revised recommendations propose enhancements to the accident and emergency unit at Ayr Hospital as soon as these can be afforded and implemented. These will include improved staffing and the redevelopment of key aspects of the unit to maintain a safe and sustainable service. These have subsequently been approved.

A public consultation about the future provision of mental health services across the area has recently been launched. Significant investment will be required in the next five years to modernise these services.

A development workshop in December 2006 identified the need for a strategic partnership “overhaul”, starting with sharing experiences and aspirations with partners via a workshop session. Management identified the need to perform a comprehensive review, particularly one involving all partners rather than a review of internal arrangements, which demonstrates good practice and the Board’s commitment to effective partnership working for patient benefit.

The original forecast outturn for 2007-08 was a surplus of £10 million, but, during the course of the year, the projected surplus outturn rose to £13 million. Management approached the Scottish Government Health Directorate for permission to carry forward this level of surplus, but this was declined. Achieving the £10 million outturn was a key challenge for management during the last quarter of 2007-08.

The capital programme included significant investment in the Crosshouse Hospital pharmacy, relocation of the paediatric department, ward upgrades, refurbishment and construction works at Ailsa Hospital, and continued investment in new electronic medical equipment and IT infrastructure. In addition, the planning and design of a new community hospital in Girvan progressed during 2007-08 with the purchase of land and commencement of the construction tender process. Through the capital grant process, and in partnership with East Ayrshire Council, the North West Kilmarnock Resource Centre opened and provides a combination of Council-led and NHS services. Work has commenced on upgrading existing facilities in Largs to provide a similar joint service.

We considered the processes and arrangements in these areas in focusing our audit effort.

Priorities and risks

KPMG’s audit methodology is risk based. To assist in the identification of risks and ensure development of a consistent approach to the audit across bodies, Audit Scotland published a *Priorities and Risks Framework* setting out seven areas for consideration:

- service redesign and sustainability;
- partnership working;
- governance;
- financial management;
- performance management;
- people management; and
- information management.

Best Value

Best Value has been part of the local government performance improvement and accountability landscape since establishment of the Best Value task force in 1997 to develop Scotland’s Best Value regime. The task force’s 2002 report led to the introduction of a formal Best Value regime for Scottish local authorities in 2003.

Following the positive impact of the Best Value concept in local government, the Scottish Ministers introduced a non-statutory Best Value duty on all public sector accountable officers (i.e. across health and central government) in 2002. Refreshed Ministerial guidance reinforced the initiative in 2006, highlighting the importance that the Scottish Government places on Best Value as a means of supporting public service reform. The Scottish Government's recent response to the Crerar scrutiny review, which credited the Best Value regime as a key driver of modernisation and improvement in public services, reinforced the requirement for robust arrangements to secure Best Value.

Audit Scotland has been committed to extending the Best Value regime across the whole public sector for some time now, with significant amounts of development work having taken place during the last year. Using the Scottish Executive's nine best value principles as the basis for activity, Audit Scotland has selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working).

These will be assessed by application by a series of toolkits, the first of which – financial management – we have piloted at the Board during 2007-08.

Responsibilities of the Board and its auditors

External auditors do not act as a substitute for the Board's own responsibilities for putting in place proper arrangements to account for its stewardship of resources made available to it and its financial performance in the use of those resources, to ensure the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the effectiveness of those arrangements and, through accountable officers, to make arrangements to secure Best Value.

We have structured the report around the headings financial statements audit, governance arrangements and performance management arrangements.

Acknowledgement

We wish to record our appreciation of the continued co-operation and assistance extended to us by your staff.

Financial statements audit

- We have issued unqualified opinions on the financial statements.
- Management considered and selected a combination of local and national assumptions in calculating the *Agenda for Change* accrual, which includes amounts due to 913 (whole time equivalents) staff not yet assimilated and the potential cost of successful reviews. The review process is at an early stage locally and nationally, so there is considerable uncertainty around the average success rate and therefore the impact on the financial position.
- A contingent liability has been reported in respect of equal pay claims as cases are at too early a stage to allow an assessment of financial risk.

Reporting arrangements and timetable

In accordance with the Board's timetable, draft financial statements were available for audit on 16 May 2008. This allowed for timely completion of the audit and consideration and approval of the financial statements by the board on 25 June 2008. In 2006-07 we made a number of suggested changes to the directors' report and the operating and financial review, some of which were actioned by management. The section of the operating and financial review on performance against national targets has been enhanced compared to 2006-07, but we have recommended and management has accepted that they should enhance the operating and financial review in future years to ensure compliance with the NHS board accounts manual.

Audit opinion

Following approval on 25 June 2008 we issued an audit report expressing an unqualified opinion on the financial statements for the year ended 31 March 2008 and on the regularity of transactions reflected in those financial statements.

Pay modernisation

The balance sheet includes *Agenda for Change* accruals amounting to £14.4 million (2007: £15.5 million). The net decrease reflects amounts paid during the year following assimilation of staff, but with increases to reflect back pay due to staff not yet assimilated, and the estimated cost of successful appeals. The nature of the accrual, particularly the latter elements, required significant management judgement to determine the assumptions on which to base the calculation. Management's evidence to support the assumptions is based on a combination of local and national statistics available in relation to the success rate of appeals processed to date. It is important that management completes the assimilation process during the early part of 2008-09 to reduce the uncertainty inherent in forecasting recurring staff costs. There is a risk that final settlement resulting from assimilation and successful appeals may be over or under the amount provided. Should this be the case, management would be required to address the matter on an in-year basis.

Recommendation one

Equal pay

Article 141 of the Treaty of Rome requires member states to ensure and maintain “the application of the principle that men and women should receive equal pay for equal work”. This was expanded on in the Equal Pay Directive, which made it clear that all such discrimination should be eliminated from all aspects of remuneration. The NHS in Scotland has received a number of claims for backdated pay increases, arising from this requirement.

For 2006-07 we accepted that no estimate of the potential liability for these claims could be identified because of the stage of development and as a result of the inclusion of a contingent liability within the financial statements. We strongly encouraged management, working with the Scottish Government Health Directorate and other NHS boards, to resolve this matter in advance of preparation of the 2007-08 financial statements.

As at 31 March 2008, NHS bodies in Scotland had received some 12,000 claims and referred them to the NHS Central Legal Office. It is possible that these claims represent a current liability for NHS boards generally. At 31 March 2008 there were 1,914 claims registered against the Board. The Central Legal Office has co-ordinated the response to all claims and attended discussions which have taken place so far. The Central Legal Office affirms that the cases in Scotland are at too early a stage to allow any assessment of financial risk to be included in the financial statements.

We note the Central Legal Office’s current view of the stage the cases have reached and management should continue to work with the Scottish Government Health Directorate and other NHS boards to form a view of the potential liabilities in line with accounting standards, taking into account the progress of cases in Scotland and in England.

Recommendation two

Corporate governance

- The statement on internal control does not disclose any significant weaknesses in the systems of internal control. The content of the SIC is consistent with our understanding and is in accordance with Scottish Government guidance.
- Internal audit have concluded that there is “*moderate assurance on the adequacy and effectiveness of the systems of internal control*”.
- There is a formal process to record, distribute and monitor action in response to key guidance and circulars, but changes in the year resulted in an incomplete register of guidance received.
- Management had inadequate arrangements in place for managing its obligations for its participation in the National Fraud Initiative, but has now established a formal process and has completed all high priority data matches, with the exception of one match currently under investigation.
- The Board met all three financial targets for 2007-08.
- The financial plan forecasts a break-even position in 2008-09 and an in-year excess of expenditure over resources of £3 million in 2009-10 to reduce the cumulative surplus to £7 million at 31 March 2010. The financial plan assumes 2% efficiency savings; achievement of which will be a significant challenge.
- The capital plan for 2008-09 assumes that the Board will incur £37.2 million of capital expenditure, which includes £10.9 million of capital brokerage. The history of incurring significant capital expenditure in the last two months of the financial year (61.3% in 2007-08) creates a risk that management will not achieve the planned outturn.

Introduction

Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour. The three fundamental principles of corporate governance – openness, integrity and accountability – apply to all bodies.

Through its chief executive, the Board is responsible for establishing arrangements for ensuring the proper conduct of its affairs, including compliance with relevant guidance, the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. The *Code* requires auditors to review and report on corporate governance arrangements as they relate to:

- the Board’s reviews of its systems of internal control, including its reporting arrangements;
- the prevention and detection of fraud and irregularity;
- standards of conduct and arrangements for the prevention and detection of corruption; and
- its financial position.

Corporate governance framework

The integrated governance framework includes four governance sub-committees of the board: audit, staff, health and performance, and clinical. The terms of reference for each committee detail decision-making powers and responsibility delegated by the board. The integrated structure is based on regular and open communication, which is enhanced by quarterly meetings of the chairs of each of the four committees.

The board consists of eight executive directors, including the chief executive, and 15 non-executive directors, including the chair. None of the members of the audit committee has an accountancy qualification.

The Ethical Standards in Public Life etc. (Scotland) Act 2000 requires NHS organisations to implement a code of conduct for board members, outlining their responsibilities. Board members make annual declarations to demonstrate compliance with these standards. In line with the model code, the code contains rules of conduct on:

- the principles of fair working, including respect and integrity;
- the receipt or provisions of gifts and hospitality;
- the register of interests; and
- confidentiality.

The Board is strengthening its governance structure through a re-focusing of the senior management team. The objective is to reflect the unified status and align the management structure with patient pathways rather than historical structures relating to the former NHS trusts.

At an operational level, the governance framework is supported by:

- standing orders outlining the roles and responsibilities of the board;
- a scheme of delegation providing information on the level of responsibility delegated to committees and employees;
- standing financial instructions that detail the financial responsibilities, policies and procedures to be adopted; and
- a set of financial operating procedures that provide detailed guidance on the operation of key processes, including financial controls, computer systems and other detailed operational workflows.

We have previously reported that, in some instances, management has not updated some of these policies for several years; management are currently developing new documents to reflect changes through time and the ongoing re-focussing exercise.

We have considered the corporate governance arrangements and, combined with the work of internal audit, concluded that the corporate governance framework has been designed and implemented appropriately, subject to timely update of operational accountability and process documents.

Statement on internal control ("SIC")

The SIC for 2007-08 provides details of the purpose of the system of internal control, the risk and control framework and the effectiveness of this framework. The director of finance, in conjunction with other senior management, prepared the SIC based on reports from internal and external audit and the risk management process. The chief executive receives assurance on the continued operation and effectiveness of the system of internal control through:

- annual reports from the four governance committees; and
- confirmation from each executive director that they are not aware of significant weaknesses in their areas of work and responsibility.

Risk management

The chief executive has overall accountability for risk management. She has delegated responsibility for the implementation of suitable and effective risk management arrangements to the director of finance. The head of clinical governance and risk management is responsible for co-ordinating, integrating, overseeing and supporting the risk management agenda and embedding risk management principles. The strategic risk group has formal terms of reference and is accountable for overseeing development, implementation and maintenance of risk management across all clinical and non-clinical functions and services. The committees regularly review risk management arrangements and receive bi-annual reports from management on key risks.

In March 2008 the board approved a revised risk management strategy, that aims to strengthen the approach to risk management and reflect the requirements of NHS Quality Improvement Scotland. The strategy builds on existing practice and aims to create a co-ordinated, systematic and focused approach to risk management. It provides a comprehensive framework, including the responsibilities of directors, staff and the board and its committees, the impact on learning and development plans, the process for an annual review of the effectiveness of risk management arrangements and relevant key performance indicators. A strategic risk management action plan is linked to the local delivery plan. The action plan and risk register demonstrate allocation of responsibilities and accountability to named individuals.

Internal audit's review of risk management arrangements in 2007 concluded that *"the common themes arising ... is the need to refine and simplify the processes to ensure officers and non-executives are focussed on the critical matters facing the organisation."* The report included three 'high' and two 'medium' priority recommendations. These recommendations were actioned during the year, including a reduction in strategic risks from 59 to under 25, a workshop on NHS Quality Improvement Scotland risk management standards, and development of the revised risk management strategy.

Clinical governance

The clinical governance strategy, which is currently under review, aims to provide the foundations on which to build and adopt a comprehensive clinical governance programme with emphasis on multidisciplinary and patient focussed improvement. The strategy defines clinical governance as *"defining and delivering continuous improvement"* and requires that *"we [the Board] do the right things, for the right people, at the right time and do them right first time"*.

The comprehensive strategy outlines the framework, including leadership roles and responsibilities, reporting arrangements, the roles and remits of the clinical governance committee and clinical governance steering group, operational and accountability links between clinical groups and other management groups, and interaction with risk management arrangements.

In partnership with NHS Dumfries and Galloway, in November 2006 the Board joined the second phase of the *Safer Patient Initiative*. The initiative, funded by the Health Foundation and delivered by the Institute for Health Improvement, brings together 20 hospitals from across the United Kingdom to work towards becoming the safest hospitals in the country and developing a national network of patient safety training sites. The initiative is a standing item on the clinical governance committee agenda, which includes status updates and performance management reports based on a balanced scorecard approach. The Board also receives regular updates, including performance achieved against set goals. The 2008-09 local delivery plan includes the safer patient clinical governance and risk management targets to ensure that these are part of the overall performance management arrangements for 2008-09. A joint board meeting with NHS Dumfries and Galloway in March 2008 developed a deeper understanding of the programme and considered the leadership role in positioning patient safety as a key strategic priority. The boards agreed a joint action plan to progress issues raised and further joint meetings are planned.

NHS Quality Improvement Scotland ("NHS QIS") published the national standards for clinical governance and risk management: achieving safe, effective, patient-focused care and services in October 2005. These standards are being used to assess the quality of services provided by NHS Scotland nationwide. NHS QIS published the results of the peer review of the Board in February 2007, concluding that "*the Board has a well-integrated risk management system at operational level and a single system risk management strategy has been approved*", that emergency planning arrangements were "*well developed*" and that a "*well-established network with partner agencies is in place*". The report highlighted weaknesses in business continuity planning arrangements, which, based on the work of internal audit during the year, have not yet been fully addressed.

The clinical governance committee's annual report considered the integration of the clinical governance and risk management with the achievement of targets and standards in the year. Key challenges in 2008-09 include the impact of the local refocusing initiative on clinical governance, NHS QIS standards and the improvements against key performance targets. The Board anticipates that it will increase its assessment rating from NHS QIS in advance of the next review scheduled for late 2009-10 and has identified standards where it will focus actions to ensure that results are strong. In 2007-08 the head of clinical governance and risk management led management in creating a "dashboard" approach to designate standards to management, identify actions to address the standards and to monitor the achievement of these standards.

Internal audit

Internal audit delivered its annual plan in full and the audit committee discussed the annual internal audit report on 18 June 2008. We placed reliance on internal audit's work, and reviewed the supporting files, in the following areas:

- budgetary setting, control and financial reporting;
- payroll and expenses;
- pharmacy stock arrangements at Crosshouse Hospital;
- risk management; and

- business continuity.

Internal audit's annual audit report concluded that there is "*moderate assurance on the adequacy and effectiveness of the system of internal control*". This is the same level of assurance as the previous year. Internal audit base their conclusion on the identification of "*mostly low and medium rated risks ... but there have been some isolated high risk recommendations*". Internal audit did not report any "critical" recommendations, but highlighted the following areas for action:

- budget setting and financial strategy – greater scrutiny of current spending patterns in the light of future funding challenges;
- business continuity planning – address concerns over the content and existence of service continuity plans at department level;
- systems and database development – review of current security and access risks in locally maintained databases;
- procurement – update the list of approved suppliers; and
- nurse bank – formally monitor the total hours worked by nurse bank staff to ensure compliance with the European Working Time Directive.

Management has agreed action plans in each area and internal audit will review progress made during 2008-09.

Internal controls

Drawing on the work of internal audit, we carried out detailed testing in relation to both organisation-wide and key financial controls. We concluded that, with the exception of perpetual stock count procedures in pharmacy and theatre stock and controls over Scottish Government Health Directorate circulars, manual journals and secondees, controls were designed appropriately and operating effectively. We also identified a number of minor areas for enhancement, including the update of standing orders, follow-up of audit recommendations, review of key reconciliations, password controls over the network and a lack of regular review of users' access rights. Management accepted the recommendations.

Our review of the controls over the reimbursement of patient travel expenses confirmed that, with the exception of the inconsistencies in the design of the processes and minor exceptions identified in sample testing of expense claims, controls are designed, implemented and operating effectively. There are however differences in practice across sites and it does not appear that patient entitlement is particularly well publicised.

Management has implemented a formal register of follow-up of recommendations raised by internal auditors, but there is no evidence that management has actioned all points and the register does not include recommendations raised by external audit.

Prevention and detection of fraud and irregularity

Fraud policy

The fraud policy is currently under review to ensure that it reflects the current operating structure. The content of the policy includes details of entity level and operational responsibility for preventing and detecting fraud and identifies mitigating controls. A fraud awareness policy and associated staff training supports the fraud policy. The head of financial services led fraud awareness sessions for staff during the year.

Management should update the policy to reflect change in management responsibilities and structure and the *Strategy to combat NHS fraud in Scotland* issued by the Scottish Government Health Directorate in January 2008.

Recommendation three

National Fraud Initiative (“NFI”)

In 2007-08 the Board participated in the NFI in Scotland. The Scottish Government Health Directorate and NHS Counter Fraud Services have strongly supported the involvement of health bodies in the exercise, which is undertaken as part of the audits of the participating bodies. NFI brings together data from health bodies, councils, police and fire and rescue boards, and other agencies, to help identify and prevent a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud and payroll fraud. Health bodies provided payroll data for the exercise. The NFI has generated significant savings for Scottish public bodies (£27 million to 2005), but if fraud or overpayments are not identified, assurances may be taken about internal arrangements for preventing and detecting fraud. Participating bodies follow up the matches, as appropriate, and record the outcomes of their investigations in the application.

The overpayments and savings identified by participating bodies in Scotland during the 2006-07 exercise is currently £9.7 million, which is likely to increase in the months ahead as bodies complete their follow-up work. While NHS boards did not identify a significant part of these savings, as they are principally responsible for payroll matches, the inclusion of NHS boards was worthwhile. NHS employees were linked with several payroll irregularities, including a significant payroll fraud involving working while on sick leave at another body. NHS employees were also linked with more than 90 cases of housing benefit fraud or overpayment. The Scottish Government Health Directorate issued guidance to all NHS boards in April 2008 to outline the requirements for data preparation and submission for inclusion in the 2008-09 NFI exercise which commences on 6 October 2008.

We monitored the Board’s involvement in NFI during the course of the 2006-07 audit, and updated our understanding of the status of investigations into data matches as part of our interim audit visit in January 2008. Our responsibilities in relation to the NFI exercise include completing a questionnaire evaluating the response to NFI. This concluded that the Board had not made adequate progress in NFI processes.

Subsequent to our observations, an action plan has been implemented, including creation of a working group. The fraud liaison officer is the NFI key contact. Operating procedures and a timetable have been created, which includes the prioritisation of high risk and higher value data matches and is supported by a detailed action plan. In April 2008 we provided a second training session on NFI to assist the staff in understanding their obligations and the process for resolution of data matches. Management has formally reported progress against the action plan to the audit committee in April and June 2008. Management has cleared all significant high priority matches, with the exception of one case that is currently under investigation.

Patient exemption checking

NHS Counter Fraud Services published the results of the 2007 patient exemption checking process in April 2008. The patient fraud protocol requires provision of an annual estimated level of fraud and error to each NHS board for the 12 months to December. The figures are based upon the results of routine checking undertaken by the patient claims team, which aims to reduce fraud by targeting higher risk areas. These results are extrapolated to produce a statistically robust estimate of total fraud within each board area and on a national basis.

Total estimated fraud within Ayrshire and Arran in 2007 is £927,000 (2006: £766,000). This represents income lost through patients fraudulently or mistakenly claiming exemptions against dental, pharmaceutical and ophthalmic treatment charges. This 21% increase is just over half the increase of the national results (44.4%). A significant proportion of the increase is due to changes in the statistical methodology used in extrapolating the results of known fraud/error. In response to our recommendation in 2006-07, management reported the results of patient exemption checking to the audit committee. We concur with management's view that the potential fraud/error is not significant and has not been reflected in the financial statements.

Regularity

In accordance with our responsibilities within *the Code*, we provide an opinion on the Board's financial statements and, as required by relevant authorities, the regularity of transactions.

In order to gain assurance over the regularity of expenditure we have updated our understanding over the processes in place to receive Scottish Government Health Directorate circulars, register, allocate and distribute responsibility for action points and monitor and follow up these action points. In 2007-08 day-to-day responsibility for the maintenance of the register changed and testing of the register and monitoring process identified that implementation of the process was incomplete. Management accepted our previous recommendation and has improved the system in recent months, but a number of circulars in relation to primary care are still not recorded in the register.

We have considered the specific requirements of a number of financial circulars, particularly those in relation to remuneration, and did not identify any instances of non-compliance.

Family health services

NHS National Services Scotland ("NHS NSS") processes family health services ("FHS") income and payments on the Board's behalf. As a result, there is no direct control over issues of systems of control and the regularity of transactions. Transactions are completed on the basis of self-certification by FHS contractors. The Board thus needs to establish appropriate governance structures and processes to verify payments made on its behalf.

Payment verification

The primary care management team, professional advisors and the head of financial services continue to meet with NHS NSS staff to discuss quarterly payment verification reports. These meetings did not identify any significant issues, but highlighted a number of areas that are subject to ongoing consideration. In response to our recommendation in 2006-07, management reported the results of patient exemption checking to the audit committee.

Qualities and outcomes framework

NHS NSS has refined and extended pre-payment verification procedures over quality payments due to GP practices under the new general medical services contract. In line with national guidance, NHS NSS visited 50% of GP practices during 2007-08 to review the prior year outturn and to provide assurance over the practices' likely achievement in the year. They randomly selected three practices for verification of quality payments; two practices achieved a high level of assurance, but records in the third practice had inadequate organisation and documentation. Management have arranged a follow-up visit to resolve these issues.

Service organisations

NHS NSS operates a number of systems and initiatives on behalf of NHS organisations in Scotland. Service auditors are appointed to provide assurance over control objectives agreed between NHS NSS and NHS boards in relation to the operation of these national systems. For the first time, service audits for 2007-08 were conducted in accordance with Statement on Auditing Standard 70, issued by the American Institute of Certified Public Accountants, in order to provide positive assurance over controls in place and to identify areas of control weakness. Audit Scotland, as external auditor of NHS NSS, reviews the work of service auditors on behalf of auditors of other NHS bodies. This has enabled us to place reliance upon the work of service auditors as follows:

- The practitioner services division of NHS NSS is responsible for calculating and making payments to primary care contractors on behalf of territorial NHS boards. The service auditor issued an unqualified opinion on 30 April 2008. Five new significant control exceptions were reported in 2007-08.
- The national logistics programme provides a centralised service for ordering, storing and distributing supplies on behalf of a number of NHS Scotland organisations. The service auditor issued an unqualified opinion in March 2008, reporting two "high risk" control weaknesses in relation to authorisation of purchase orders and the creation of new suppliers.
- NHS NSS manages a range of national information and management technology systems that underpin delivery of the eHealth strategy and are integral to the operations of NHS bodies. The service auditor issued an unqualified opinion in March 2008. Two "high risk" control weaknesses were identified, relating to awareness of password policies and documentation of 'known errors' referred to service teams.
- Audit Scotland performed an additional review of NHS NSS arrangements to manage the national information management and technology infrastructure. This review highlighted a small number of risk areas but concluded that overall management arrangements were adequate.

Financial position

The Board achieved all three of its financial targets for 2007-08.

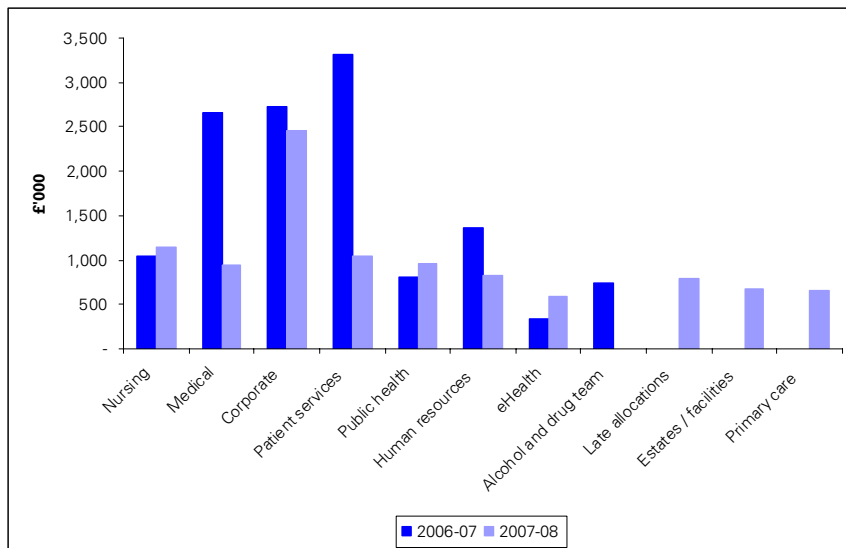
The original forecast outturn for 2007-08 was a surplus of £10 million, but, during the course of the year, the projected surplus outturn rose to £13 million. Management approached the Scottish Government Health Directorate for permission to carry forward this level of surplus, but this was declined. Achieving the £10 million outturn against the revenue resource limit agreed with the Scottish Government was a key challenge for management during the last quarter of 2007-08. The actual outturn at 31 March 2008 was £9.961 million, reflecting an in-year excess of expenditure over resources of £3 million.

The most significant single reason that management secured the outturn against the required revenue resource limit was due to changes in the funding of impairment. Initially, management had anticipated an additional allocation of £4.4 million to meet the costs of impairment and minor capital expenditure. During the final quarter of the financial year the Scottish Government Health Directorate confirmed that the additional allocation would only be £1.9 million, requiring funding of the remaining £2.5 million from internal resources. The Board received income and incurred expenditure proportionately and in line with budget throughout the year, with none of the key service categories deviating from a consistent quarterly pattern.

In 2006-07, net operating costs included £3.5 million of non-recurring expenditure. This pattern continued in 2007-08 when net operating costs included in excess of £5 million of non-recurring expenditure. There is a risk that, when the Board is required to utilise funding carried forward, the recurring cost base increases in excess of the Board’s recurring funding allocations. In 2006-07 and 2007-08 management has utilised a significant proportion of funding carried forward for non-recurring purposes, which is likely to reduce, but not eliminate, the risk of recurring overspends in future years.

A comparison of the elements of the carry forward in 2006-07 and 2007-08 is shown in figure one.

Figure one: funding carry forward 2006-07 and 2007-08



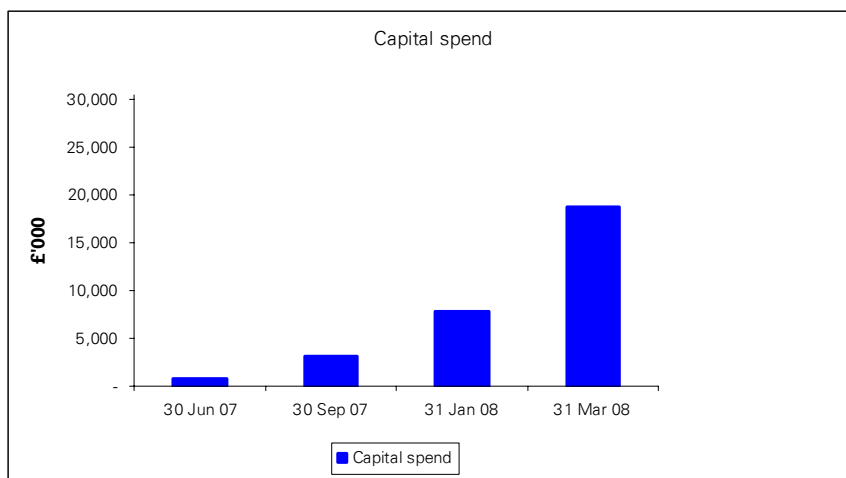
Source: Ayrshire and Arran NHS Board 2007-08

The only individually significant element of carried forward funding relates to bridging finance, which accounts for £2.4 million (2006-07: £2.5 million) of the ‘corporate’ carry forward. At 31 March 2008, management has not earmarked 23% of the £9.961 million and will use these funds to meet non-recurring cost pressures in 2008-09.

Capital expenditure equalled the capital resource limit for 2007-08 of £30.4 million. The Board incurred significant expenditure on estates maintenance projects (£8 million), electro-medical equipment (£5.6 million), the Largs resource centre (£3.3 million), Afton House (£2.8 million), information management and technology projects (£2.7 million), the pharmacy at Crosshouse Hospital (£1.7 million) and Mossblown Clinic (£1.1 million). The profile of capital spend during the year is shown in figure two.

The Board achieved its capital target due to significant (£18.6 million, 61.3%) expenditure in February and March 2008 and approval of carry forward funding. The Scottish Government Health Directorate has approved brokerage of £10.9 million, of which £6.2 million relates to unspent allocations in 2006-07, allowing the Board to carry this forward into 2008-09. £4.7 million of the total brokerage arose in 2007-08, primarily due to delays in prioritising and commencing capital projects following the service review process that resulted in retention of accident and emergency services at Ayr Hospital.

Figure two: capital spend profile 2007-08



Source: Ayrshire and Arran NHS Board 2007-08

The Board's ability to carry forward capital funding into 2009-10 is likely to be limited, thus requiring management to maximise spend in 2008-09. Management should ensure that sufficient focus and resources are applied to capital planning and spend throughout 2008-09 to mitigate the risk of a similar spend profile to 2007-08, which could have a significant impact on the Board's ability to meet the challenging capital resource limit of £37.2 million.

Recommendation four

Financial plans

The 2008-09 financial plan forecasts a break-even position in 2008-09 and an in-year excess of expenditure over resources of £3 million in 2009-10 to reduce the cumulative surplus to £7 million at 31 March 2010. Management has identified specific recurring cost pressures for 2008-09, including the expected three-year pay settlement, incremental drift in *Agenda for Change* pay scales, and inflation in pharmacy costs.

The board approves the budget setting process on an annual basis prior to approving the annual and three-year financial plan. The budget setting process, which includes input by clinicians and managers outwith the finance department, is weakened considerably by the lack of consideration of base budgets; the focus is on allocation of funding uplifts and new monies available. The absence of a budgeting approach that considers existing budgets on a cyclical basis results in the risk that existing budgets may not be appropriate for current service provision. Management are currently reviewing existing processes with a view to re-basing budgets in 2009-10. We have considered financial management processes during our pilot of Audit Scotland's Best Value toolkit 'use of resources – financial management' and will report on this area in due course.

The 2008-09 financial plan requires management to identify and achieve 2% efficiency savings. Historically, achievement of financial plans has not been dependent on achievement of savings, due to allocation uplifts averaging over 7% during the last six years. Management anticipate that allocations will be uplifted by around 3% per annum for the next three years. Consequently, management face significant challenges in funding recurring and non-recurring cost pressures, while achieving 2% efficiency savings, and achieving the 2008-09 financial plan.

The review of services process has delayed approval of the ten-year capital plan and start dates for projects at Ayr and Crosshouse Hospitals. Key developments at these sites include a combined assessment unit and extension of renal capacity, either through extension of existing Crosshouse facilities or development of a new satellite unit at Ayr. During 2008-09 management expect approval of a capital plan identifying £289 million of capital expenditure over nine years, including the mental health service review, Ayrshire Central community hospital, a new community hospital in Girvan, critical care services at Ayr and Crosshouse hospitals, and unscheduled and emergency care facilities at Ayr and Crosshouse hospitals.

Performance management

- Development of acute services and mental health facilities will depend on achievement of financial plans and challenging efficiency targets. A culture change will be required to ensure that cash released through efficiency savings is directed and prioritised appropriately.
- 913 whole time equivalent staff (8%) were not assimilated by the year end. Assimilated staff had lodged 2,000 review requests, but management has not yet completed any reviews.
- There are significant workforce and financial challenges due to high absence levels. Management has developed a number of local initiatives to monitor the impact of sickness absence and 'promote attendance', but sickness absence rates remain high at 5.6%.
- A 'strategic alliance' between the Board and three councils aims to improve partnership working at a strategic level. Management has prepared a draft engagement plan to outline key deliverables and milestones, to be developed further in the summer of 2008.
- Management had identified significant risks to achievement of delayed discharge and three other key targets (staff absence, emergency re-admissions and cancer waiting times) in 2007-08. The corporate management team recognised that achievement of these targets required organisational commitment at all levels across all disciplines. While the delayed discharge target was achieved, the other 'at risk' targets were not.
- Our review of the Board's information management arrangements confirmed that, subject to finalisation and implementation of information security management arrangements, processes are in place to mitigate the risks in this area.
- Management established a 'benchmarking, efficiency and sustainability' team, responsible for providing leadership, direction and support for efficient government initiatives and projects, while balancing this with sustainability.
- There is clear awareness and acceptance of competing financial and strategic pressures, but the way in which this change will be managed and implemented, strategically and financially, is not always clear and consistent across the organisation. Clear commitment and direction from top management will be crucial to the achievement of strategic and financial objectives in coming years.
- Delays in identifying and implementing efficiency schemes will have a significant impact on the ability to meet 2% savings targets in 2008-09 and achievement will depend on implementation of a robust mechanism to identify, record and report savings achieved.

Service developments

The Cabinet Secretary established an Independent Scrutiny Panel ("ISP") to provide a view on whether the revised unscheduled care proposals in relation to the retention of accident and emergency services at Ayr Hospital, would be:

- safe, sustainable, evidence based and represent value for money;
- robust, patient-centred and consistent with clinical best practice and national policy;
- reflective of local circumstances and the views of individuals and communities affected; and

- comprehensive in terms of considering all viable options.

The Board, in conjunction with Lanarkshire NHS Board, independently appointed third party advisors to provide independent project assurance in relation to the project management arrangements. In addition, the independent review provided commentary on the application of HM Treasury's Green Book principles to the option appraisal process and the Board's reporting and decision-making process.

The advisors provided verbal and written feedback to management throughout the engagement and issued a final report in January 2008, narrating their findings and commenting to the board on the processes and procedures followed. The advisors considered the following key documents, in addition to supporting project management documentation:

- the first submission to the ISP (September 2007);
- ISP interim report (October 2007);
- scoring packs for the benefits scoring events (October 2007); and
- ISP draft final report (January 2008).

We have considered the work completed by the advisors and held a series of meetings during the course of their engagement to update our understanding of the process and the emerging findings. We have also considered papers produced by the Board and the ISP.

The independent advisors concluded that:

- project management arrangements were appropriate given the time constraints relating to the project;
- notwithstanding the issues raised, the Board followed the fundamental principles of HM Treasury's Green Book in undertaking its option appraisal;
- the board has been kept advised of developments through formal board meetings and informal seminars, but due to time constraints the board did not have sight of the final version of the first or second ISP reports before they were submitted; and
- detailed minutes of discussions and decisions were recorded and the decision-making practices had been reasonable during the process.

In arriving at its decision on the future of accident and emergency services, the board considered the options available to it and noted the comments from the range of reports and evidence. The overall aim was to ensure the continuation of accident and emergency services at Ayr Hospital, while delivering as many as possible of the enhancements to other services described in the previous review of services, as agreed in October 2006.

The revised scheme proposes enhancements to the accident and emergency unit at Ayr Hospital as soon as these can be afforded and implemented. As a result, a review of all acute service proposals and a prioritisation exercise for both revenue and capital funding is underway to determine the impact of the Cabinet Secretary's decision on other service requirements. The board has stressed that implementation of proposals is dependant on achievement of the 2% recurring efficiency savings from 2008-09.

Following establishment of the mental health programme board in 2007, there has been an ambitious programme of stakeholder involvement through a series of engaging, participative workshops, working groups, reference groups, public information sessions and conferences. In January 2008 support for the overarching model of care and for the proposed approach to planning inpatient mental health services was confirmed. A period of wider engaging and informing with patients, the public and staff around the recommendations finished in April 2008.

The option appraisal process regarding the location of inpatient mental health services commenced in November 2007 and will be complete in October 2008 after a period of formal consultation around a short list of options. The board is currently considering detailed analysis of the informing and engaging activities undertaken by the 'mind your health' project against the requirements of national guidelines.

A paper submitted to the board in January 2008 identified £9.25 million of desired developments in community based mental health services. In addition, proposals for new in-patient accommodation will require additional capital and revenue funding. The additional funding required will depend on the outcome of ongoing option appraisal and public consultation. Similar to the outcome of the review of acute services, development of mental health facilities will depend on achievement of financial plans and challenging efficiency targets. Mental health services have not been reviewed since the mid-1990s and, in recent years, acute services have received the majority of development funding. The culture at operational level, continues to show a divide between the services formerly provided by the acute and primary care NHS trusts. This creates an additional challenge for management and a culture change will be required to ensure that cash released through efficiency savings is directed and prioritised appropriately.

Workforce management

Managing full implementation of the pay modernisation agenda, particularly *Agenda for Change* and the knowledge and skills framework ("KSF"), continues to progress. By 31 March 2008 913 whole time equivalent staff (8%) had not been assimilated, although 157 of these staff were assimilated in the first two months of 2008-09. Assimilated staff had lodged 2,000 review requests, but management has not yet completed any reviews. The staff governance committee received an update on KSF, which highlighted that 78% of outlines have been completed at 31 March 2008. HEAT targets in 2008-09 require all staff in the scope of *Agenda for Change* to have an agreed KSF personal development plan by March 2009.

Implementation and ongoing monitoring of pay modernisation initiatives requires significant resource input, particularly by payroll and human resources staff. During 2007-08, management explained that a lack of resources resulted in delays in full assimilation under *Agenda for Change* and lack of timely progress in discharging obligations in relation to the National Fraud Initiative. Despite the time taken to assimilate employees, management believe that a relatively high proportion of review requests will be successful. It is important that management considers the resources required to ensure that initiatives are implemented and monitored on an ongoing basis in a timely and accurate manner.

Recommendation five

The staff governance committee, area partnership forum, senior management team and board considered the annual staff governance submission in March and April 2008. Management has completed an action plan, including priorities, responsible officers and implementation timetables, and will report progress to the staff governance committee.

We have identified risks over people and workforce management, including weaknesses in the links between strategic and workforce planning, pay modernisation, the age profile (which is higher than the national average) and service redesign plans. Management continue to address these, but plans may take a long time to implement.

There are significant workforce and financial challenges due to high absence levels. Management has developed a number of local initiatives to monitor the impact of sickness absence and 'promote attendance', but sickness absence rates remained high at 5.6% at 31 March 2008. The Scottish Government recently announced that achievement of the 4% target is required at 31 March 2009, rather than the previous deadline of 31 March 2008. This remains a key challenge to ensure that the 4% is achieved together with £1 million savings on nurse bank and medical locum costs.

Partnership working

A development workshop in December 2006 identified the need for a strategic partnership "overhaul", starting with sharing experiences and aspirations with partners via a workshop session. The Board has identified partnership working as a key development area and should ensure that appropriate and sufficient resources are available to implement agreed actions to achieve the vision of 'creating a sustainable future'. At the time of establishment in April 2005, it was agreed that the CHP model would be subject to review during 2006-07. The review commenced at the end of 2006-07 and continued throughout 2007-08. It has identified a need to perform a comprehensive review, particularly one involving all partners rather than a review of internal arrangements. This demonstrates good practice and the commitment to effective partnership working for patient benefit.

A status report in April 2008 identified the next steps and proposed timeline for completion and the associated stakeholder engagement plan. This plan includes the initial results of the 'strategic alliance', between the Board and three councils which has been created to improve partnership working at a strategic level. Management has prepared a draft engagement plan to outline key deliverables and milestones, which will be developed further in the summer of 2008.

The resource transfer agreement between the Board and the three councils is renegotiated on an annual basis, but the agreement has not been formally documented since 2001. Our review of the controls over resource transfer agreements with the three councils confirmed that controls are designed, implemented and operating effectively, but arrangements should be formalised to protect the Board's financial and performance interests.

From 2008-09 delayed discharge funding will be allocated directly to local authorities and will not be ring-fenced. There is a risk that the Board is accountable for meeting targets, but does not have financial control, particularly when dealing with three local authorities, each with different priorities and financial pressures.

The area partnership forum ("APF") annual report highlighted key changes in the structure of the APF at the beginning of the year, which resulted in a reorganisation of the local partnership forums on a geographical basis rather than the former NHS trust structure. The APF has been actively involved in the Board's decision-making and approval process during the year, including the review of services, mental health redevelopment, CHP restructuring, *Agenda for Change* and KSF.

Performance management

Management use a balanced scorecard to monitor and report performance against health improvement, efficiency, access and treatment (“HEAT”) targets on a monthly basis. The health and performance governance committee considers detailed reports on high profile targets. In addition to the local delivery plan, management prepare an annual operational plan, which includes a combination of HEAT targets and other business indicators.

During preparation of the 2007-08 local delivery plan management identified significant risks to achievement of delayed discharge and three other key targets (staff absence, emergency re-admissions and cancer waiting times). The corporate management team recognised that achievement of these targets required organisational commitment at all levels across all disciplines. The delayed discharge target for 2007-08 was achieved, but the other ‘at risk’ targets were not achieved. The operating and financial review provides information on all HEAT targets where the Board’s performance was more than 5% away from the target.

In approving the local delivery plan 2008-09 the chief executive of NHS Scotland highlighted the need for management to:

- manage key existing and emerging financial risks to ensure achievement of financial targets;
- develop and strengthen the link between service improvement and reducing risks of non-achievement of HEAT targets;
- achieve shorter waiting times during 2008-09 to minimise risk to the achievement of the 18 week ‘referral to treatment’ target in 2011; and
- consider the workforce implications of meeting HEAT targets in 2008-09 and future years.

Information management

The eHealth strategic planning process ensures that consideration of information management and technology is part of short and long-term objectives and strategic planning. Consistent management of third party services and implementation of appropriate key performance indicators as part of the IT project management process could enhance the performance management framework.

An internal policy and requirements in employment contracts govern information security, but this could be strengthened by implementing annual staff re-declaration of the policy. There is an identified control weakness surrounding the restriction of sensitive data storage within portable media. The board should ratify the draft policy to govern the issue as soon as possible. There is no existing organisation-wide policy on encryption.

Each area within the Board is responsible for developing and maintaining a business continuity plan. An information security policy document provides high-level guidance around business continuity management and a number of plans and testing regimes are in place. There is a lack of awareness within the service user departments of responsibilities around business continuity management, including the lack of a periodically tested Board-wide plan.

Our review of the Board’s information management arrangements confirmed that, subject to finalisation and implementation of information security management arrangements, processes are in place to mitigate the risks in this area. Management accepted our recommendations in this area.

Audit Scotland performance studies

Audit Scotland undertakes a programme of studies on financial management, governance and performance on behalf of the Auditor General. This programme covers topics of national importance. During 2007-08 the following reports were published in relation to the NHS:

- primary care out-of-hours services;
- overseas staff in the NHS – pre-employment checks;
- overview of Scotland’s health and NHS performance in 2006-07;
- free nursing and personal care; and
- managing long term conditions.

Studies on NHS asset management, diagnostics, mental health, national general medical services contract and palliative care are in progress. Audit Scotland expects to publish the NHS overview report 2007-08, focusing on financial management, in December 2008.

The chief executive receives reports and distributes them to relevant senior management. Where management detailed actions are required, an internal action plan is prepared. The audit committee receives all reports, of which some are subject to detailed discussion and others are noted and subject to full discussion by another governance committee such as clinical or staff governance.

Overseas staff in the NHS – pre-employment checks

Events in Glasgow and London in 2007 were alleged to involve overseas staff working in the NHS. Following these incidents reviews were instigated which covered the arrangements for recruiting overseas staff for work in the NHS. In Scotland the Cabinet Secretary for Health and Wellbeing also requested a review of whether pre-employment screening of overseas staff working in the NHS in Scotland was in line with guidelines set out by the Centre for Protection of National Infrastructure.

Audit Scotland carried out a review as to whether NHS boards are following their own procedures on pre-employment screening, reporting in November 2007. This review considered whether NHS boards, including Ayrshire and Arran NHS Board, were complying with pre-employment screening procedures for overseas staff and included testing source documentation in five NHS boards.

Audit Scotland reported a high level of compliance and, from a sample of 235 files across five NHS boards, there was evidence on files to demonstrate that 75% of checks were performed. The Board had one of the highest numbers of non-European Economic Area staff in the sample. Recommendations over the receipt of work permits and the performance of disclosure checks were applicable to the Board. The organisational and human resources department has responsibility for ensuring that the report’s recommendations are actioned so that adequate procedures are in place.

Asset management

The NHS in Scotland owns assets valued at over £4 billion including land, hospitals and equipment. The way these are managed has a significant impact upon service delivery. The NHS is currently undergoing service redesign which will also have an impact on the way assets are managed. The overall aim of the study is to consider the extent to which the NHS manages its assets strategically in order to ensure they are used as efficiently and effectively as possible. The study will highlight areas of good practice and make recommendations where assets can be used more efficiently.

Management has discussed the requirements of the review and the director of finance will complete and submit the data request to Audit Scotland in July 2008. Audit Scotland plan to publish their report in the autumn of 2008.

Review of major capital projects in Scotland

Between 2002 and 2007, the Scottish Government and its agencies, non-departmental public bodies and the NHS completed 43 publicly funded major (in excess of £5 million) capital projects valued at £811 million. Audit Scotland's report was published in June 2008 and highlighted the following key messages:

- in general, the achievement of cost and time targets improved significantly as time progressed;
- early cost and time estimates at project approval stage were too optimistic for many major projects;
- cost and time performance is made better after contracts are awarded, as plans are more certain and risks clearer;
- few projects have been evaluated to demonstrate that they have delivered the expected wider benefits which originally justified the investment; and
- a more strategic approach to managing capital projects could improve value for money.

Best Value

Audit Scotland's 2005-06 baseline review of arrangements assessed the Board's position in six out of the ten underpinning Best Value characteristics as 'well developed'. Three of the remaining four areas were assessed as 'under development' and 'a contribution to sustainable development' was assessed as 'planned'. A number of actions were subsequently agreed and progressed in 2006-07 and 2007-08.

Members of the corporate management team are individually assigned areas assessed as 'under development' for development and action. Management established a 'benchmarking, efficiency and sustainability' team during 2007-08, a multi-disciplinary group responsible for providing leadership, direction and support for efficient government initiatives and projects, while balancing this with sustainability.

2008-09 onwards

Audit Scotland has been committed to extending the Best Value audit regime across the whole public sector for some time now, with significant amounts of development work having taken place during the last year. Using the Scottish Executive's nine best value principles as the basis for audit activity, Audit Scotland has selected five areas as priority development areas (use of resources, governance and risk management, accountability, review and option appraisal, and joint working). Audit Scotland is currently developing a series of toolkits that auditors will be required to use from 2008-09. Completion of these toolkits will require a detailed examination of arrangements in specific areas.

The focus of this work in 2008-09 will be on the use of resources, including efficiency, information management, procurement, asset management, performance management and people management. It is anticipated that national reports may be prepared by Audit Scotland and it is therefore important that the Board ensures that appropriate focus and resources are available to develop arrangements to secure Best Value.

Use of resources – financial management

We are piloting the first Best Value toolkit and have completed our fieldwork. Following a moderation process with Audit Scotland, we will report our findings during 2008-09. At the time of this report, the high level results of our work demonstrate an awareness of the current and changing financial and strategic environment and the consequent need to change the financial management culture within the organisation. Service provision in the acute and mental health sectors is subject to current review and the results of will require increased investment in specific areas and service redesign. These changes will be required during a period of less than anticipated funding increases, the need to achieve efficiency savings and increased pressure to meet financial plans on a year by year basis. While there is clear awareness and acceptance of these competing pressures, the way in which this change will be managed and implemented, strategically and financially, does not always appear clear and consistent across the organisation. Clear commitment and direction from top management will be crucial to the achievement of strategic and financial objectives in coming years.

Efficient government

The efficient government initiative is a five-year programme with the aim of tackling waste, bureaucracy and duplication in Scotland's public sector. NHS boards need to embrace the efficient government agenda and establish a clear programme for delivering efficiency savings.

The 2007-08 year-end outturn included achievement of £5.52 million of efficiency savings against a target of £5.24 million. Management has reported significant savings in the cost of supplies, property rationalisation, safer patient initiatives and staff costs from vacancy management.

Management initially identified a need for efficiency savings of 4% in 2008-09, based on the Scottish Government's 2% requirement together with a local target of 2%. Management recognised the challenges it faced in securing a 4% efficiency savings target set for 2008-09 and established a 'benchmarking, efficiency and sustainability' team. All support and service departments were requested to identify local initiatives to achieve 4% efficiency savings. In first responses, support services reached the 4% target, but service departments only identified savings of less than 1%. The total identified at this stage was only £4 million; less than 1% of total budgets. Following the response to the 'bottom-up' approach, management adopted a top-down approach to identify £7 million of savings to ensure achievement of at least the Scottish Government's 2% target.

Management has reduced operational budgets by £11 million to reflect the savings to be achieved, but service departments have not yet identified specific schemes within these areas. Identification of specific schemes is required to mitigate the risk of overspends against budget. Delays in identifying and implementing efficiency schemes will have a significant impact on the ability to meet savings targets in the first year. Management should ensure that a robust mechanism of identifying recording and reporting efficiency savings is implemented without delay.

Recommendation six

Management estimate that £10 million of the £11 million savings will release cash for service development. £1 million of savings will reduce overspends in nurse bank and medical locum costs. Management has allocated the £10 million across service priorities, including mental health services (£2.8 million) and pay modernisation (£2 million).

National shared support services

During the period to January 2007 NHS Scotland has been developing proposals for shared support services in financial and related services in the form of a “hub and spoke” model. The response to the proposals, including that from the Board, was characterised by reservations over the risks inherent in the proposed scheme, the impact on staff and the deliverability of savings. The project was subsequently re-launched as the shared support services programme, involving a two-tier approach which seeks to build confidence in new ways of working, using common processes and systems, leading to a single services model based on a common finance system.

This approach involves a “foundation” level of involvement around common ledger arrangements, or a “pathfinder” approach which seeks to develop more advanced elements. NHS National Services Scotland, on behalf of the Scottish Government Health Directorate, published a paper on the shared support services programme ‘plan for the way forward’ in September 2007. This paper clearly outlines the aims and objectives of the project in the period to March 2009 and beyond.

In 2007-08, the Board approved and implemented a proposal to establish and lead a consortium, which consists of Lanarkshire, Dumfries and Galloway, Shetland, and Orkney NHS Boards, NHS Health Scotland, and NHS Education Scotland. The financial services consortium management team oversees the project and includes representatives from all member boards. This team meets on a monthly basis and receives and consider a project update, updates on the national shared services programme, and risk management. A risk register and action plan exists at consortium and local NHS board level.

The Board implemented a new version of the financial ledger and a standard chart of accounts in April 2008. The implementation was well managed and users reported only minor issues over interfaces with the financial ledger and reporting.

Appendix – action plan

Priority rating for performance improvement observations raised		
<p>Grade one (significant) observations are those relating to business issues, high level or other important internal controls. These are significant matters relating to factors critical to the success of the Board or systems under consideration. The weakness may therefore give rise to loss or error.</p>	<p>Grade two (material) observations are those on less important control systems, one-off items subsequently corrected, improvements to the efficiency and effectiveness of controls and items which may be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified.</p>	<p>Grade three (minor) observations are those recommendations to improve the efficiency and effectiveness of controls and recommendations which would assist us as auditors. The weakness does not appear to affect the availability of the controls to meet their objectives in any significant way. These are less significant observations than grades one and two, but we still consider they merit attention.</p>

No.	Issue and performance improvement observation	Management response	Officer and due date
1	<p>It is important that management complete the assimilation and appeals processes during 2008-09 to reduce the uncertainty inherent in forecasting recurring staff costs.</p> <p>There is a risk that final settlement of resulting from assimilation and successful appeals may be over or under the amount provided. Should this be the case, management would be required to address the matter on an in-year basis.</p> <p><i>(Grade two)</i></p>	<p>Management believe a prudent provision has been made, but this will be monitored closely in 2008-09.</p>	<p>Director of finance Ongoing</p>
2	<p>We note the CLO's current view of the stage the equal pay cases have reached and management should continue to work with the Scottish Government Health Directorate and other NHS boards to form a view of the potential liabilities in line with accounting standards, taking into account the progress of cases in Scotland and in England.</p> <p><i>(Grade one)</i></p>	<p>We will work with the equal pay unit which has been established nationally.</p>	<p>Director of finance Ongoing</p>
3	<p>Management should update the fraud policy to reflect change in management responsibilities and structure and the 'strategy to combat NHS fraud in Scotland' issued by the Scottish Government Health Directorate in January 2008.</p> <p><i>(Grade two)</i></p>	<p>Agreed.</p>	<p>Fraud champion 31 December 2008</p>

No.	Issue and performance improvement observation	Management response	Officer and due date
4	<p>The Board's ability to carry forward capital funding into 2009-10 is likely to be limited, thus requiring management to maximise spend in 2008-09.</p> <p>Management should ensure that sufficient focus and resources are applied to capital planning and spend throughout 2008-09 to mitigate the risk of a similar spend profile to 2007-08, which could have a significant impact on the Board's ability to meet the challenging capital resource limit of £37.2 million.</p> <p><i>(Grade two)</i></p>	Agreed.	<p>Head of capital planning and facilities</p> <p>Ongoing</p>
5	<p>Implementation and ongoing monitoring of pay modernisation initiatives requires significant resource input, particularly by payroll and human resources staff. Despite the time taken to assimilate employees, management believe that a relatively high proportion of review requests will be successful.</p> <p>It is important that management considers the resources required to ensure that initiatives are implemented and monitored on an ongoing basis in a timely and accurate manner.</p> <p><i>(Grade two)</i></p>	An assessment of capacity required and priority of each initiative will be done as they emerge.	<p>Director of finance</p> <p>Director of organisational and human resources development</p> <p>Ongoing</p>
6	<p>Delays in identifying and implementing efficiency schemes will have a significant impact on the Board's ability to meet savings targets in 2008-09.</p> <p>Management should ensure that a robust mechanism of identifying recording and reporting efficiency savings is implemented without delay.</p> <p><i>(Grade one)</i></p>	The efficiency savings for 2008-09 have been identified, reported to the finance committee and deducted from budgets at source. In-year emerging overspends will be closely monitored.	<p>Director of finance</p> <p>Ongoing</p>

